DOW THEORY LETTERS INC.

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Registered with the Securities Exchange Commission

40 Letters per Year — $50.00 Annually

THE MARKET: I am often asked what my biggest problem is in regard to writing these Letters. My unhesitating answer is "space!" I have written the first part of this Letter in two sections: (1) an orthodox Dow Theory market discussion, and (2) a copious quantity of fact and opinion (formulated from constant reading of what I consider to be the most intelligent and knowledgeable sources available). In order to conserve space I have taken the liberty of deleting (with this issue only) the regular Chart 1 showing the advance-decline ratios on the N.Y.S.E. and the Amex. As of this writing the A-D ratio on the Big Board is again trying to do what it has not been able to do for 16 months — namely, better its May, 1963 peak. The current effort may be successful, but it is worth remembering that we are again in the area from which breadth (the A-D ratio) turned down in May, 1963, September, 1963, April, 1964 and July, 1964. While the A-D ratio continues its grim struggle on the N.Y.S.E., all we can say about the breadth performance on the more speculative Amex is that it is providing more of the same lackluster performance which has characterized its action since 1962.

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In August the Industrials refused to confirm the Rail weakness. At that time (Letter 263) I wrote: "Many important advances have materialized from areas in which one Average persistently refused to confirm a penetration of the other. Now (six weeks later) it is obvious that the stubborn refusal by Industrials to display weakness (on the downside) during August gave way to selective but "surprising" September strength (on the upside).

Again, however, the Dow Theory confirmation principle assumes significance. On September 8 the Industrial Average climbed above its July 17 peak, thereby rising into historic high ground. Anticipating this, I noted in the last Letter (264): "In the event of a new all-time Industrial high (above 851.35) it will be most important to see whether Rails confirm by bettering their own all-time high of 220.98."

A glance at Chart 2 will show that although Industrials have recovered all their July-August losses and have surged into new high territory, Rails have been reticent. This is all the more interesting because it represents the first time since October, 1962, that Rails have been the laggers. From the bullish viewpoint, it would be well to remember that there have been many instances in the past when one or the other Average trailed behind — only to catch up in due time. From the bearish standpoint, it should be noted that many (in fact almost all) important declines have stemmed from areas in which one Average persistently refused to confirm the bullish indications of the other.

CONCLUSION: Watch the Rails. If they move along in an upward direction with Industrials, all may continue well — if not rosy. But if Rail weakness is so pronounced that the carriers actually start parting ways with Industrials, be careful. History shows that few movements last very long unless both Averages continue in the same direction — as if locked "in gear."

* * * * *

In this writer's opinion, the period ahead promises to be increasingly exciting for market students. From all sides we are told that "all is well." "NO MAJOR DISTORTIONS" is the headline adorning a highly respected market letter which arrived here today. A number of

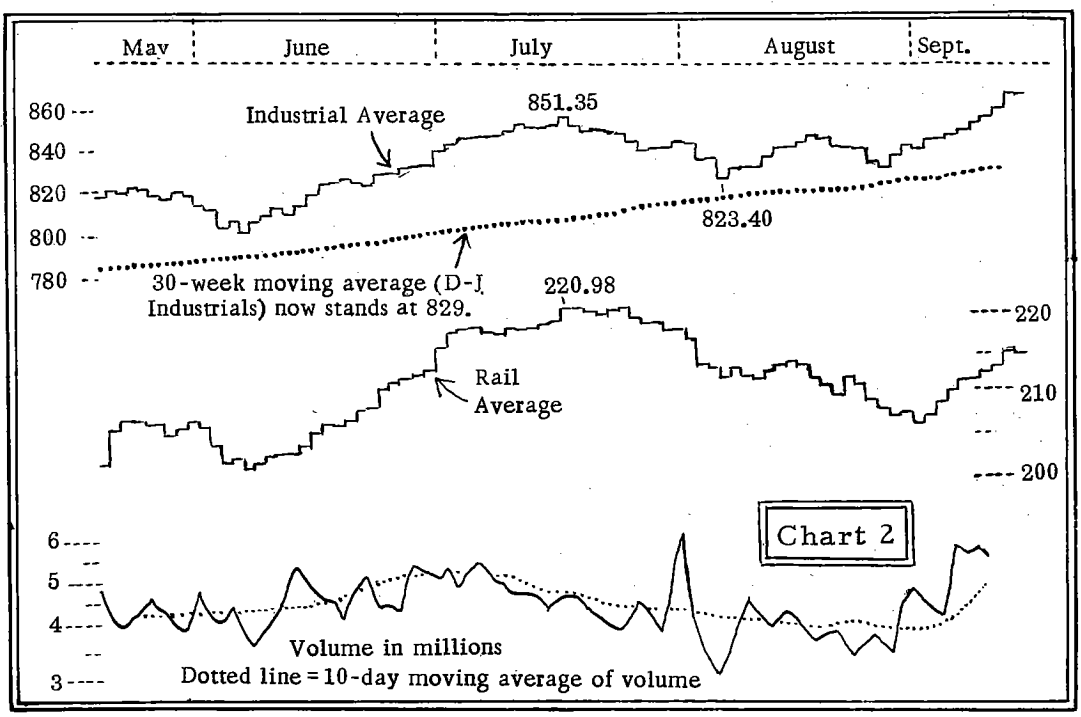


Chart 2

leading analysts are predicting a final "blow-off" for the post-World War II bull market which will take us profitably into early or mid-1965. But others are uneasy. From a veteran subscriber comes this note, written on the margin of a bullish brokerage house forecast: "In some 35 years working with the market, I have never seen such comforting assurances from all directions that we are all going to have abundant opportunity to get out at the top 'next year' with nothing but green pastures betwixt now and then." (R.B.N., Houston, Texas).

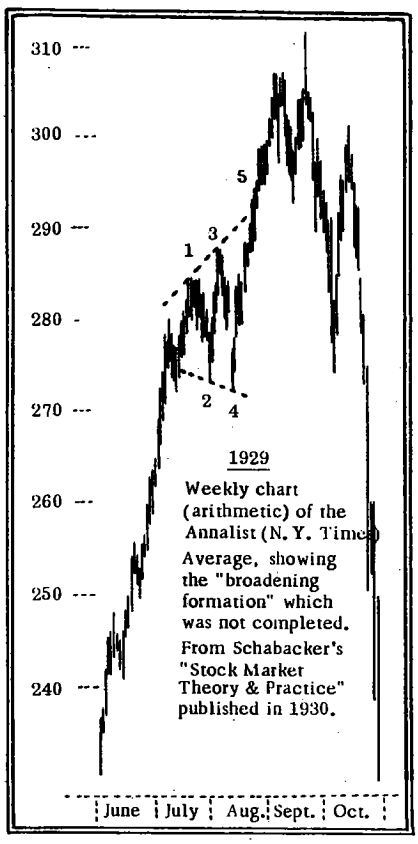
If there is a major "distortion" haunting our market, I am convinced that it exists within the world of international money (see Letter 260). London, in fact, may be leading the way to a world mess. The pound is in trouble, and the trouble is worsening. Britain is now financing (lending on 15-year terms) large Russian purchases. As economist Eliot Janeway puts it: "The British are underwriting the Russians as if the city of London were still banker to the world. But the grim fact is that the once proud and stable pound sterling is being buffeted and battered by a potential devaluation crisis so grave that only massive emergency advances of dollars can keep it above water. The spectacle of Britain borrowing on this side of the Atlantic by day while leading on the other side of the curtain on a 15-year span would be comical — if it weren't so serious."

The Free World's commerce runs on the two major reserve currencies — the pound and the dollar. With the pound touching new lows daily, world commerce is turning increasingly to the dollar. The grim fact is that the U. S. dollar is being used (with a resultant one to two billion dollar annual deficit here) to feed cash into Europe in an effort to avoid a major money squeeze and crisis there. The dollar scarcity in Europe is now reaching extremely serious proportions. This dollar shortage has lead to a fantastic velocity of lending, re-lending, arbitrage, manipulating, and financing overseas. Such nations as Britain and Japan have built an incredible pyramid of "cards," all predicated on their ability to obtain and turn over the scarce American dollars.

How does all this effect us? When a motor is roaring at utmost capacity, any minor defect may blow it wide. Europe and the Free World are running on a boom which is being financed by American dollars — dollars that are growing frighteningly scarce. When a crack does appear, the repercussions are likely to be sudden and drastic. The possibility of skyrocketing interest rates, British devaluation, a collapsing bond market, a Japanese crisis, any of these (or something from an even more "remote" area) could start important trouble. My own opinion and conclusion: Keep the major portion of your funds in U. S. Treasury Bills. Speculate if you must, but "tread lightly" and remember that if a money crisis does strike, it will stop the boom and the stock market dead in its tracks (and it will then be almost impossible to sell large amounts of stocks).

THEN AND NOW: I have received many letters from subscribers asking for further comments on the "broadening pattern" which has been evident in the Industrial Average. Since the writer makes it a practice of telling subscribers exactly what he is thinking about and "mulling over," I will confess that I have been making certain comparisons between 1929 and the present.

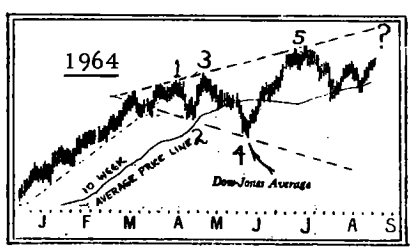
In 1929 the New York Times (the old Annalist) Average traced out a "broadening formation," a pattern which was not completed at the time. The great analyst and Editor of Forbes Magazine, Richard Schabacker, discussed this extraordinary phenomenon in his book (see accompanying chart). After noting that "it looked very much as though a broadening top was being formed during this period, to signal the major reversal of the long bull movement," Schabacker observed that the extraordinary market, following leg 5 (see chart) pushed higher instead of turning down as might have been expected. Thus the broadening pattern was not completed, and the leg which began at point 4 extended to new all-time highs.



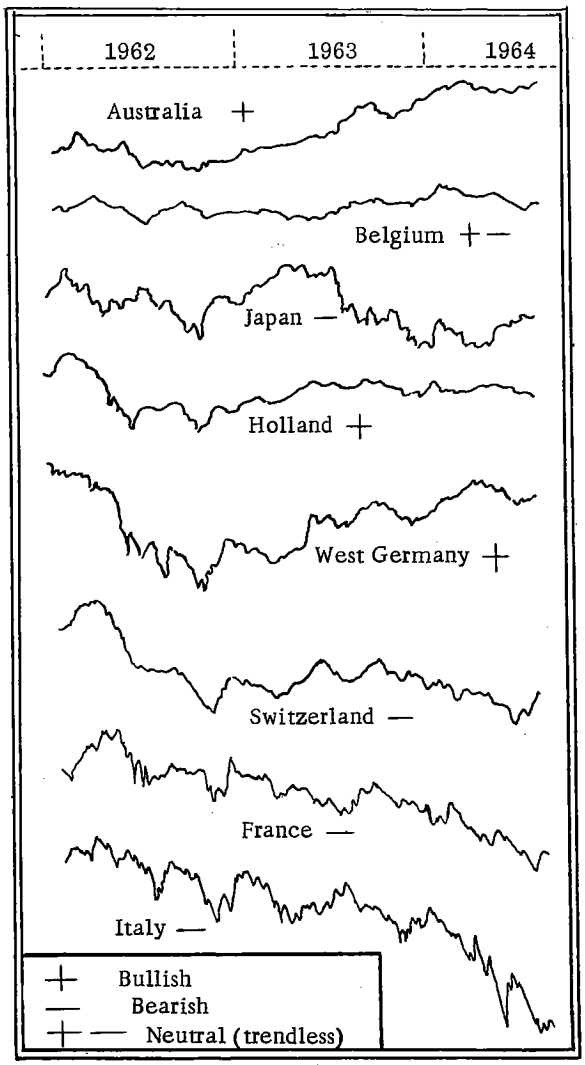
1929
Weekly chart (arithmetic) of the Annalist (N.Y. Times) Average, showing the "broadening formation" which was not completed. From Schabacker's "Stock Market Theory & Practice" published in 1930.

The warning was there, however, as is so often the case following a bearish technical pattern which does not materialize at once. Subsequent to the August penetration of the upper trendline of the potential broadening top, the market continued higher for two months — then crashed. In retrospect, it is probable that the "swirling excitement" which formed the rare broadening pattern of 1929 was also the type of excitement which customarily appears near the end of a bull market.

What of the picture today? In the opinion of the writer, the appearance of the broadening pattern during 1964 is a phenomenon which should be noted and remembered. Such patterns are extremely rare. The 1929 broadening effect turned out to be a major distributive pattern. This writer suspects that the 1964 pattern represents "a horse of very much the same color," and although the market may push higher from here, technical analysis has already issued an important warning.



FOREIGN MARKET: It was Robert Rhea (writing in the 1930's) who observed that during primary movements and most secondary movements the markets of the world tend to move together. This writer was one of the first to offer periodic discussions of the world markets, and I have found that what the markets of the Free World do — as well as what they do not do — is usually quite significant.



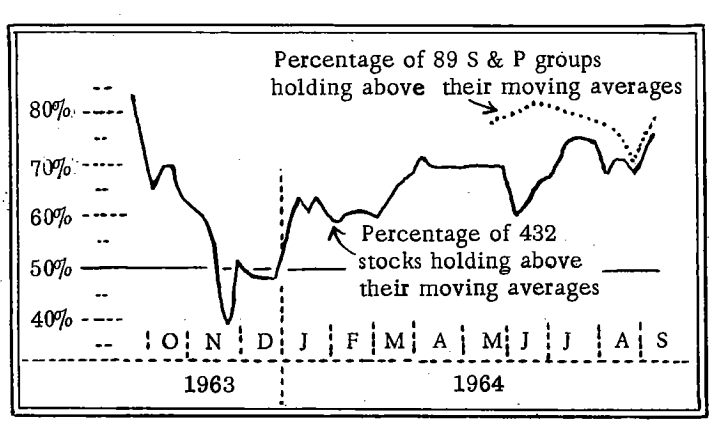
Up to 1960-61, the world market picture was quite bullish. But from 1960-61 to the present the markets of the Free World have presented a decidedly "mixed bag." In my own mind I have wondered whether the picture since 1961 has not corresponded with the view put forth by a few astute analysts (Mr. Hamilton Bolton of Canada is one) who hold that the "true post-war bull market peak" probably occurred in 1961, and that although the D-J Averages have continued to push higher, many stocks and indices have already seen their "tops." This view is not as farfetched as it may seem, for we know that the majority of issues (as measured by the advance-decline ratio) turned down in the late 1950's, just as the majority of issues touched their peak in late 1928 — a full year before the 1929 crash.

A review of the foreign markets would seem to further fortify the thesis that the true peak of the post-World War II boom has already passed. The Australian Average (see accompanying chart) is one of the world's strongest and is currently at its bull market high. The Belgian stock Average has been moving sideways within a narrow range for almost four years. Japan's stock Average saw its bull market peak in late 1963. Since then the famed Japanese "people's market" has headed violently down (although the last few months have produced a rallying trend on this Exchange). The important Dutch market reached its bull peak in 1961, broke badly in 1962, recovered during early 1963, and has flattened out or sagged slightly ever since.

West Germany saw its bull market peak as early as 1960. The German market broke badly in 1962, and since then it has been in a recovery phase (although not as strong as the recovery seen in the U. S.). The Swiss market touched its peak in 1962 and has been heading generally lower ever since. France's market has brought no pleasure to Gaulic investors, the most recent action having taken the French average to another major new low. Italy possesses the dubious honor of having produced the first market crash of the post-World War II era. Subsequent to the 1960 crash on the Italian Exchange, that market moved up to a secondary peak in 1962, then (under the threat of Communism and chaos) the Italian market moved steadily into new low ground.

The foreign averages depicted on the chart are all drawn to the same semi-logarithmic scale; therefore they may be compared with each other as far as percentage of advance or decline is concerned. I classify (see plus or minus marks on chart) four of the leading world markets as bullish (Britain not shown is bullish), one as neutral, and four as bearish. All of which suggests that international money is not having any easier time of it than the fellow who is now trying to pick "a winner" on the N. Y. S. E.

STOCKS: Of 432 representative stocks tabulated here weekly, 329 (76%) are now holding above their 200-day or long term moving averages -- a rise of 8% since the last Letter (this study remains bullish as long as the "count" is above 50%). Of 89 Standard & Poor stock groups, 70 (79%) are holding above their M. A.'s, a rise of 11% since the last reading (see accompanying chart).


Percentage of 89 S & P groups holding above their moving averages
80%
70%
60%
50%
40%
Percentage of 432 stocks holding above their moving averages
O N D J F M A M J J A S
1963
1964

QUESTION: You seem to believe that we are coming closer and closer to the end of the entire post-World War II boom. The great Dow Theorist Robert Rhea wrote that he would have been more than satisfied if he could have executed all his purchases within 10% of a bull market bottom and sold out within 10% of a bull market top. Assuming the Industrial Average were to rise to 950 or even 1000 during the next three to six months,

this still would be around the "10% from the top" thesis as put forth by Rhea. Following this line of cautious reasoning, why do you even bother to suggest stocks for purchase in this area?

ANSWER: (1) I have stated (on numerous occasions) that I do not believe this market is anything but a trading proposition. The long-term investor is concerned with safety, values, attractive yields, an early position in the cycle, buying conditions which are dull and devoid of crowd interest; none of these conditions have been present for years. Quite the contrary, everything about this market suggests that long-term investors should now be thinking in terms of unloading and assuming a cash position.

(2) Nevertheless, I do have readers, old and new, amateur and veteran, who want to speculate and do not mind assuming the risks. These men buy stocks with their eyes open, fully aware of the dangers which are inherent in a 15-year old bull market. I feel that my speculative-minded readers may be able to improve their "batting average" with some of the stocks which I discuss in these Letters. In the final analysis, I would rather have readers pick a "depressed" Burroughs or Callahan Mining than a "glamorous" Pan American Airways or IBM (the latter two bought, perhaps, at the peak of their bull market cycles).

(3) Finally, my job does entail keeping track of and analyzing hundreds of stocks (and stock groups). This means that I am bound to come up with certain groups and issues which look interesting. A good group or a strong stock will often do well in any but a broad declining market. I feel that if I come up with something interesting — then my subscribers are entitled to know about it. Furthermore, many of the stock discussions in these Letters are presented with the idea of teaching subscribers what to look for and why. (I will also confess that there is a certain pleasure in knowing that many readers own a stock, purchased on the basis of a recommendation here, which is outperforming the market).

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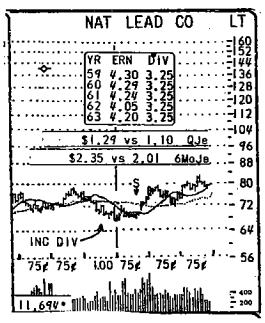
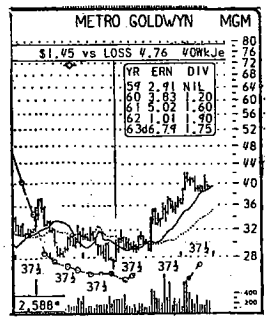
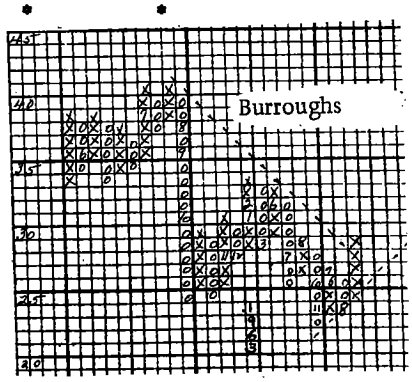
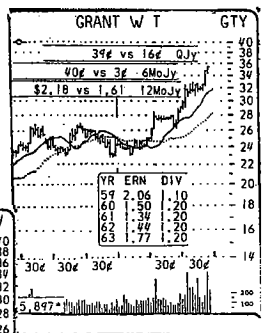
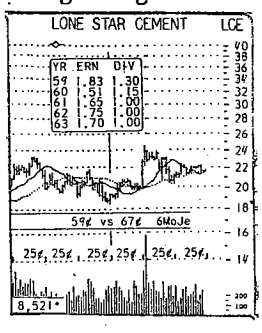


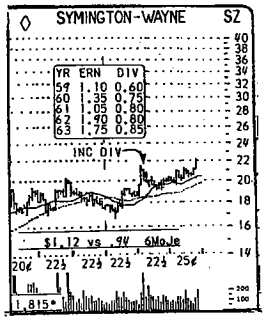




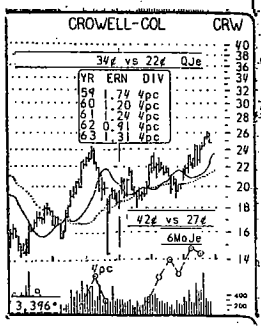
REVIEW: Many recent recommendations have been doing quite well. Burroughs (Letter 257) has finally attracted some fund buying; the latest three months show that 20,000 shares of BGH have been purchased by funds. The importance of the recent action in BGH is brought out on the accompanying point & figure chart which shows that a bullish "breakout" in BGH at 28 and a complete reversal of the bearish trendline at 29. Hold this stock; it is outperforming the group (which is now weak) and the market. MGM (Letter 259) has reacted back to its 10-week moving average (solid line on chart), and continues to look O. K. National Lead (Letter 259), after being recommended at 78, pushed out 83, then sank back to its 10-week M. A. (see chart). Stock still acting all right.

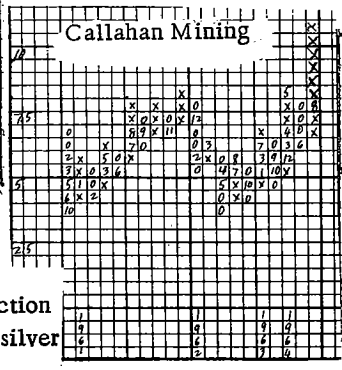


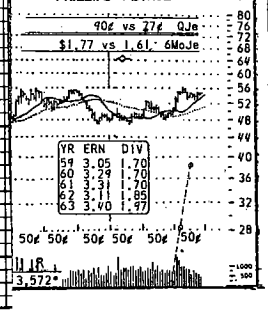


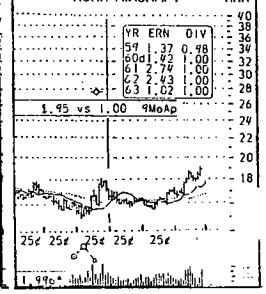


W. T. Grant (Letter 259) acts outstandingly well and touched a new high this week. Symington-Wayne (Letter 260) now at an all-time high, but a "following" still does not build up in this one. Lone Star Cement (Letter 260) is "sitting" and has neither made nor lost money for anyone yet. Phillips Petroleum (Letter 262) convertible bonds act well, and the common shows good fund accumulation. Rohr convertibles (Letter 262) also look good, having gained a few points from where I recommended them. Rohr stock now strongly bullish. Crowell-Collier (Letter 262) has been bringing in a little fund and insider buying, and the common is behaving quite well. The tremendous breakout in Callahan Mining (Letter 248 and frequently thereafter) is seen on the point & figure chart. All the action since 1961 now constitutes a huge base for this one. The silver "play" has been the "kicker" behind CMN.

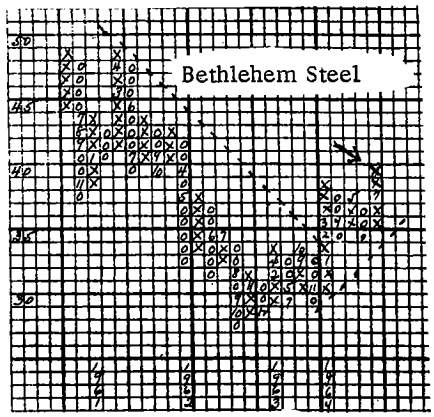




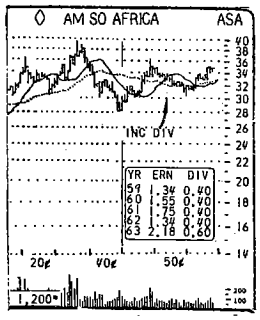




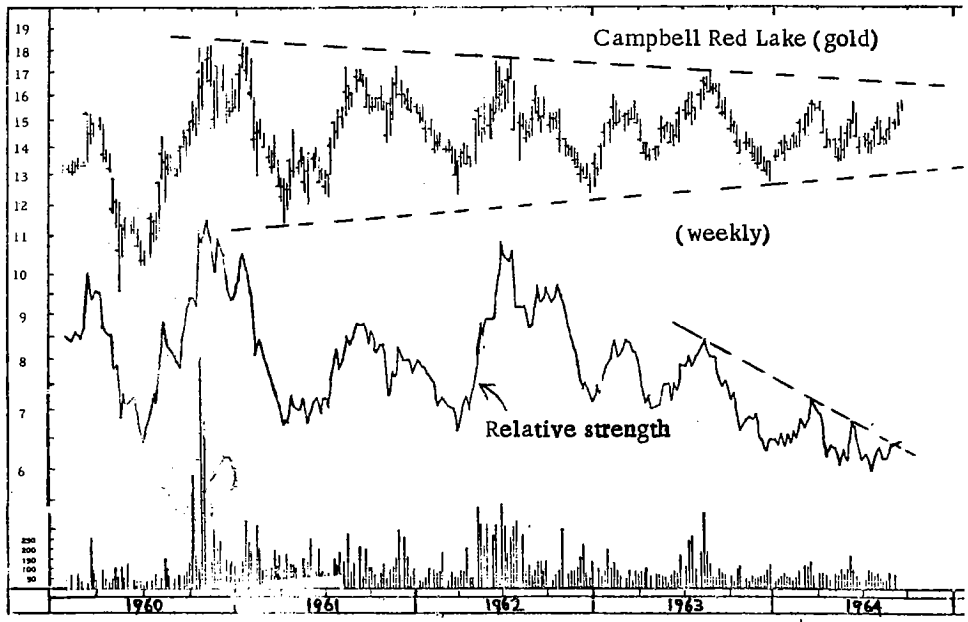
Bethlehem Steel (Letter 264) touched 40 this week, thus providing a new "buy-signal" on the basis of the point & figure chart. Funds bought $ 8 million worth of BS over the past 3 months, and the stock acts quite well (see Letter 264).



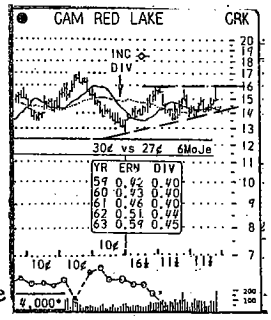
Above are a good portion of the "speculative recommendations" of the past few months. But the investments, in my opinion, have been discussed many times in these Letters (and last in Letter 263). The investments are the golds. When governments tinker with money, men's minds automatically turn to thoughts of gold. Furthermore, with the gathering British sterling crisis and its possible implications for the dollar, it is little wonder that the gold stocks have been moving.

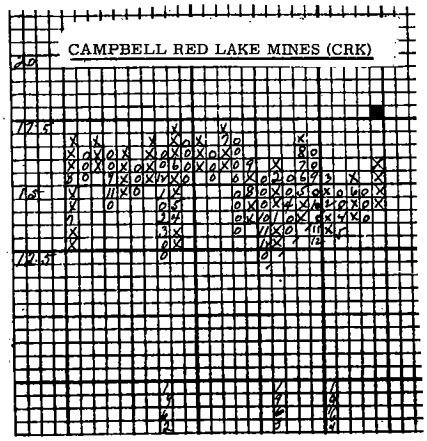


I last recommended golds in Letter 263. American South African has done well, and is approaching the critical 37 point. If it hits 37 (see small weekly chart), I would add to previous commitments (be sure on all golds to tell your broker that you want an American affidavit attached — to avoid possible new tax). Dome (Letter 264) has now pushed above all peaks for the year and may be heading for the critical 34 high of 1963. DM has been recommended many times in these Letters.

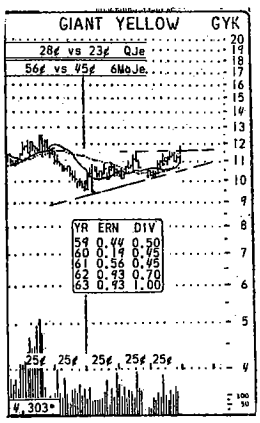


This week I am suggesting purchases of Campbell Red Lake Mines and Giant Yellowknife. As seen on the large weekly chart, Campbell (CRK) has formed an absolutely incredible four year triangle. Its relative strength line is beginning to push above a long declining trendline. On September 14 CRK touched 16, thus registering a point & figure "buy signal" (see chart) by bettering two previous tops. Main objective for CRK is 18, a point which would signal a probably massive rise in CRK and the entire gold group (the 18 point is marked with a black square on the P & F chart). Note on small weekly chart that CRK has formed a bullish ascending triangle over the past few months, and it was this triangle which was bettered on September 14. CRK is holding well above its 200-day M. A. which now stands at 14 1/2.

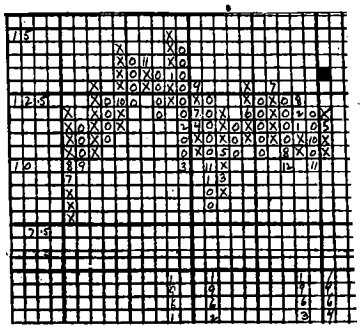




Giant Yellowknife on the Amex pays a dividend of $1. This week (see small weekly chart) GYK broke above an ascending triangle, thereby joining the rest of the golds on the upside. The P & F chart shows 13 1/2 (black square) as the important bull point for GYK. Touching this, it will have only the 1962 peak of 15 ahead of it. I list both CRK and GYK as excellent stocks to buy and hold. In my opinion, it is not a question of "whether" a big move in golds — it is "when."



GIANT YELLOWKNIFE GOLD (GYK)



Large chart of CRK courtesy of Traders Research, 1431 Pearl Ave., Alton, Illinois 62003. All small weekly charts courtesy of Quote Digest, 110 N. Lorraine, Wichita, Kansas. P & F chart courtesy of Chartcraft, Larchmont, N. Y.

This Letter completed 10 A. M. September 15, 1964 (Tuesday).